

TEACHERS' RETIREMENT BOARD

INVESTMENT COMMITTEE

SUBJECT: External Equities – Semi-annual Equity Manager Report ITEM NUMBER: 11

ATTACHMENT(S): 1

ACTION: _____

DATE OF MEETING: October 2, 2002

INFORMATION: X

PRESENTER(S): Elleen Okada

Executive Summary

Attached is the semi-annual equity investment performance evaluation report for the period ended June 30, 2002. This report is intended to assist the Committee in their oversight of staff's delegated authority. The report includes the performance information on the aggregate portfolio level within U.S. and Non-U.S. equity. The report was developed using audited performance data from the CalSTRS' custodian, State Street Bank. The Chief Investment Officer (CIO) or designee has delegated authority to manage the equity portfolio and hire, retain, and terminate individual investment managers within the parameters established in the external equity policy and asset allocation guidelines as approved by the Board. This report is designed to provide the Board with a comprehensive review of the active equity portfolio.

Background

The external equity staff utilizes a number of sophisticated software programs to help dissect an individual manager's performance. These programs include Barra Analytics, Vestek, and Zephyr Style Advisor. Additionally, staff meets with the external managers twice a year minimally, at CalSTRS and at the managers' offices. These on-site visits help staff understand the managers' "corporate culture." This understanding increases staff's ability to interpret changes to the managers' investment process. The steady pace of investment manager mergers and personnel departures increases the need to understand how subtle changes could affect the managers' performance.

Attachment 1 provides graphic displays of the level of changes in the capital markets, and the performances of U.S. equity managers and Non-U.S. equity managers. Also presented is an overview of staff's analysis of the portfolios relative to the appropriate benchmarks. This attachment includes the following:

- a) Returns for the Russell 3000 and the MSCI ACWI indices for the last three years.
- b) U.S. and Non-U.S. major market returns for 6 months, 1 year and 3 years ending June 30, 2002.
- c) CalSTRS' U.S. equity structure compared to the Russell 3000 on June 30, 2002.
- d) CalSTRS' U.S. equity aggregate portfolio returns for 6 months, 1 year and 3 years ending June 30, 2002.
- e) CalSTRS' Non-U.S. equity structure compared to the MSCI ACWI ex U.S on June 30, 2002.
- f) CalSTRS' Non-U.S. equity aggregate portfolio returns for 6 months, 1 year, 3 years and 5 years ending June 30, 2002.
- g) Glossary.

Summary

CalSTRS' U.S. active equity managers have significantly out performed the Russell 3000 ex-Tobacco benchmark on an aggregated basis over six months, one year and three years by 442, 546 and 341 basis points, respectively. The decision made in 1997 to increase the use of active management and the selection of managers has helped the portfolio out perform the benchmark. In aggregate, the U.S. active equity managers have exceeded staff's expectations.

The success of the Non-U.S. active equity portfolio has also been strong. The Non-U.S. active managers out performed the MSCI ACWI ex-Tobacco benchmark over six months, three years and five years by 74, 191 and 439 basis points, respectively. However over the one year period, the Non-U.S. active equity managers under performed the benchmark by 30 basis points.

In closed session, staff will present the rating of each manager. This rating gives consideration to both quantitative and qualitative factors.



Executive Summary of the External Equity Managers' Investment Performance

Semi-Annual Period Ending June 30, 2002

Table of Contents

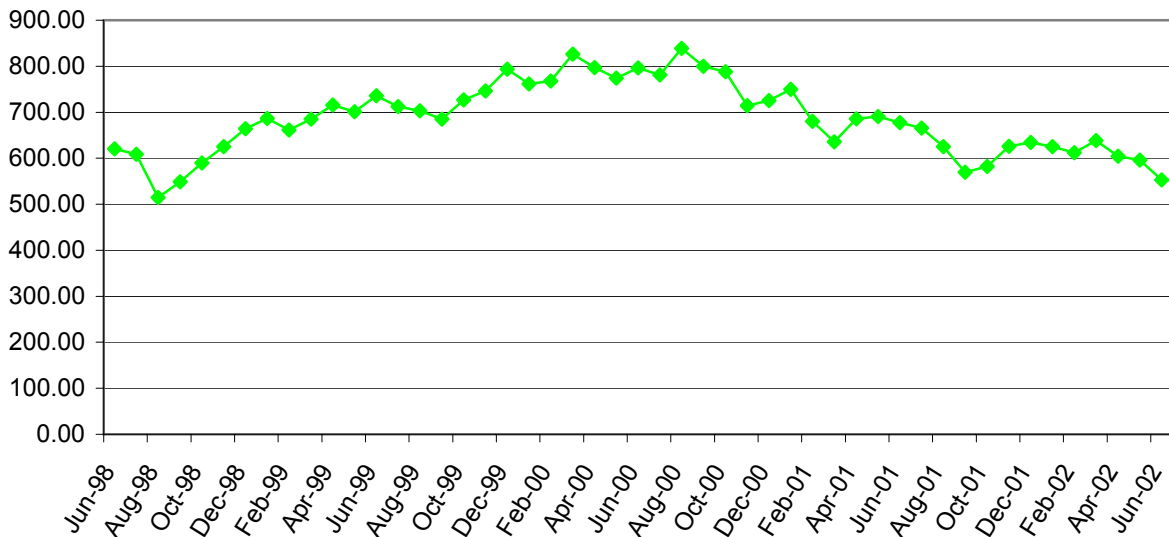
Capital Market Environment.	1
U.S. Equity Portfolio Structure.	4
U.S. Equity Aggregate Level Investment Performance.	5
Non-U.S. Equity Portfolio Structure.	8
Non-U.S. Equity Aggregate Level Investment Performance.	9
Glossary	11

Based on Audited data from State Street Bank

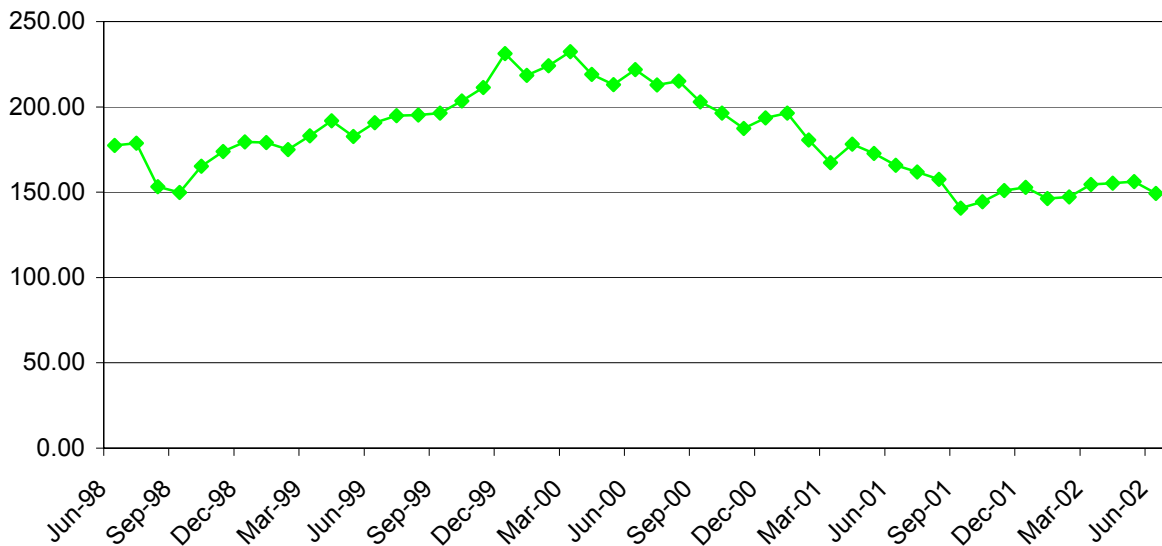


Capital Market Environment

Russell 3000 June 1998 - June 2002



MSCI ACWI Free Ex US June 1998 - June 2002

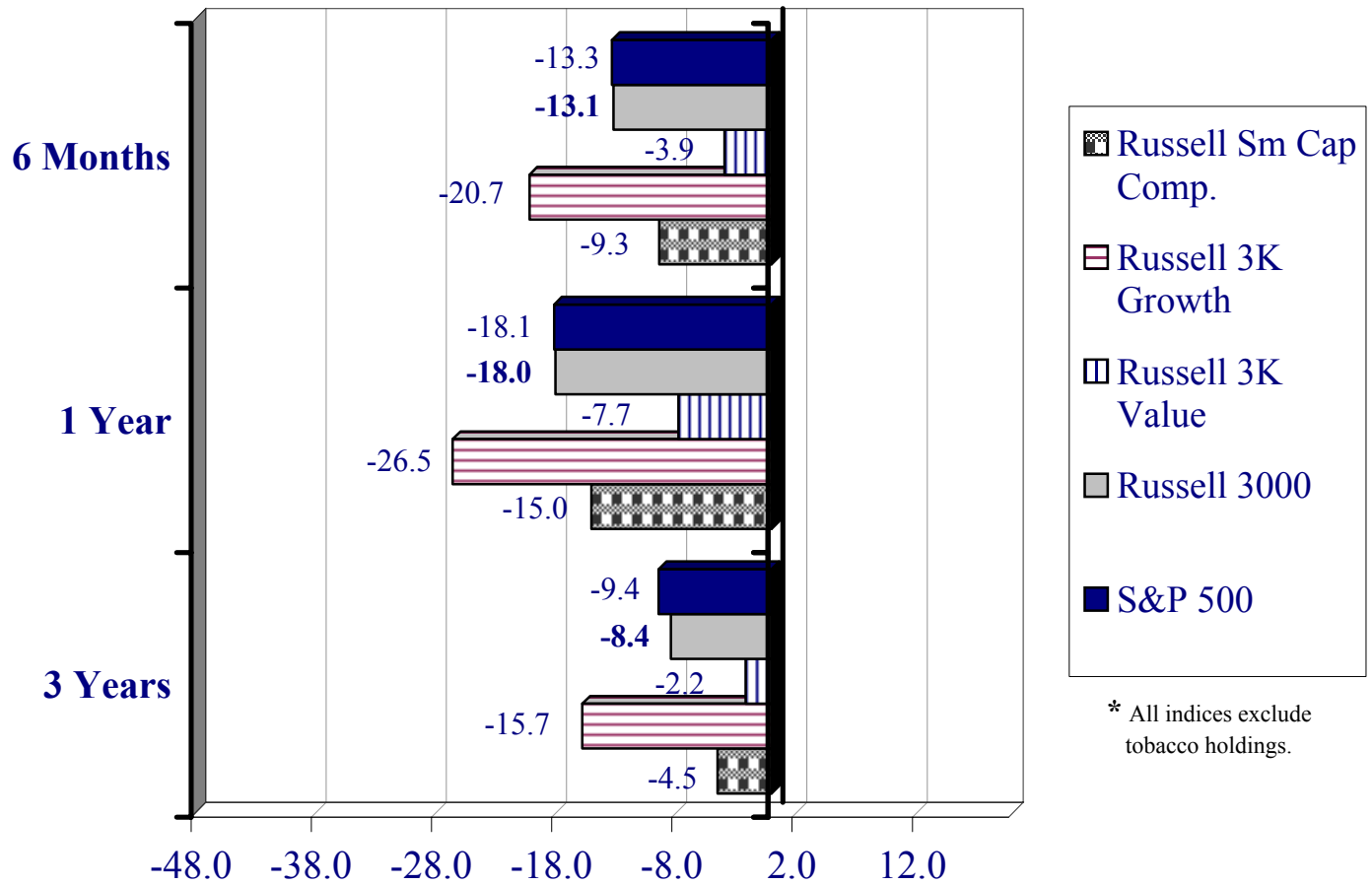




Capital Market Environment

U.S. Equity Market Returns 6 months, 1 year, and 3 years ending June 30, 2002

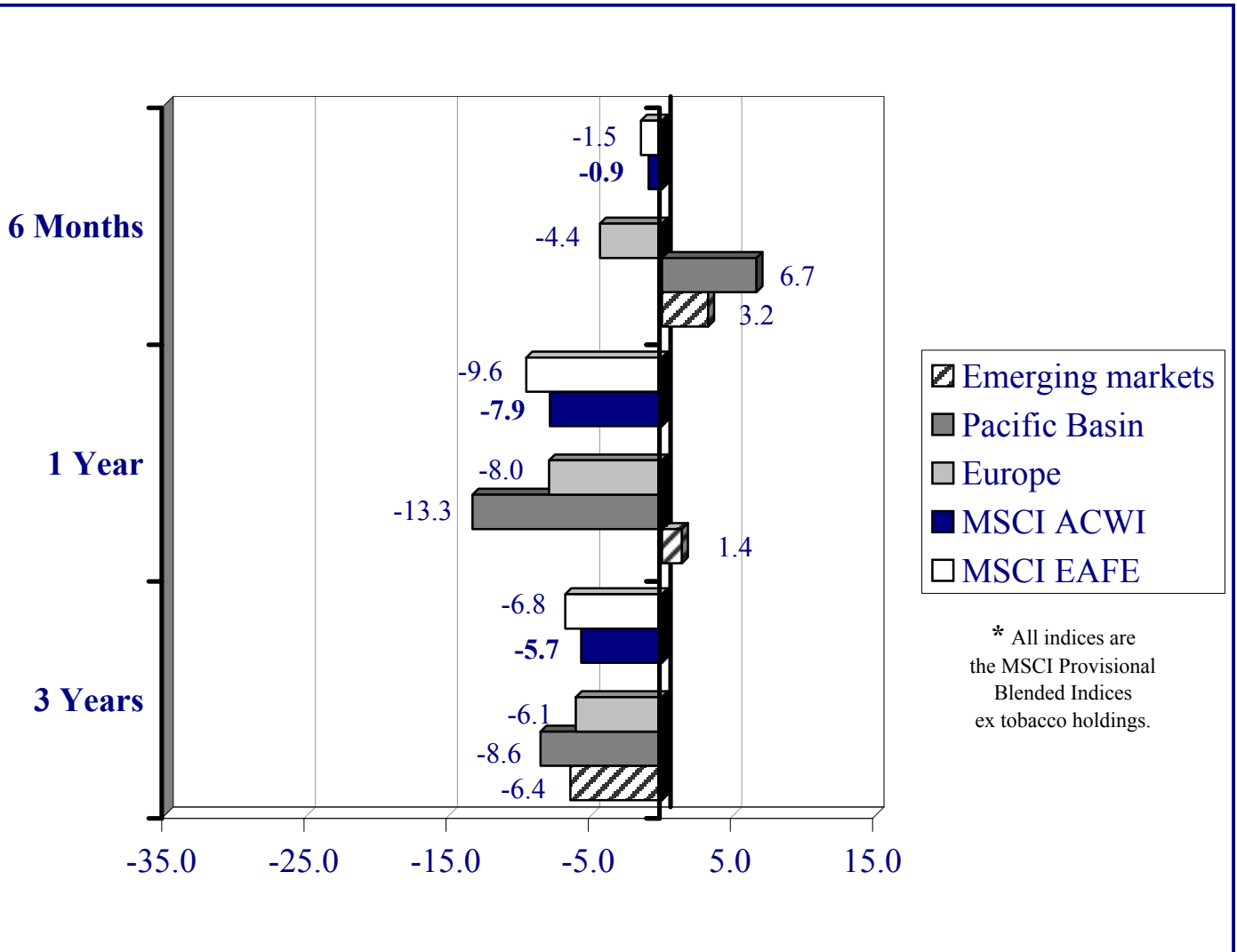
	6 Months	1 Year	3 Years
S&P 500	-13.3%	-18.1%	-9.4%
Russell 3000	-13.1%	-18.0%	-8.4%
Russell 3K Value	-3.9%	-7.7%	-2.2%
Russell 3K Growth	-20.7%	-26.5%	-15.7%
Russell Sm Cap Comp.	-9.3%	-15.0%	-4.5%



Capital Market Environment

Non-U.S. Equity Market Returns 6 months, 1 Year, and 3 Years ending June 30, 2002

	6 Months	1 Year	3 Years
MSCI EAFE	-1.5%	-9.6%	-6.8%
MSCI ACWI	-0.9%	-7.9%	-5.7%
Europe	-4.4%	-8.0%	-6.1%
Pacific Basin	6.7%	-13.3%	-8.6%
Emerging markets	3.2%	1.4%	-6.4%





U.S. Equity Portfolio Structure

Russell 3000 Structure

	Value	Core	Growth
Large Cap	32.0%	29.2%	31.7%
Small Cap	2.5%	2.4%	2.2%

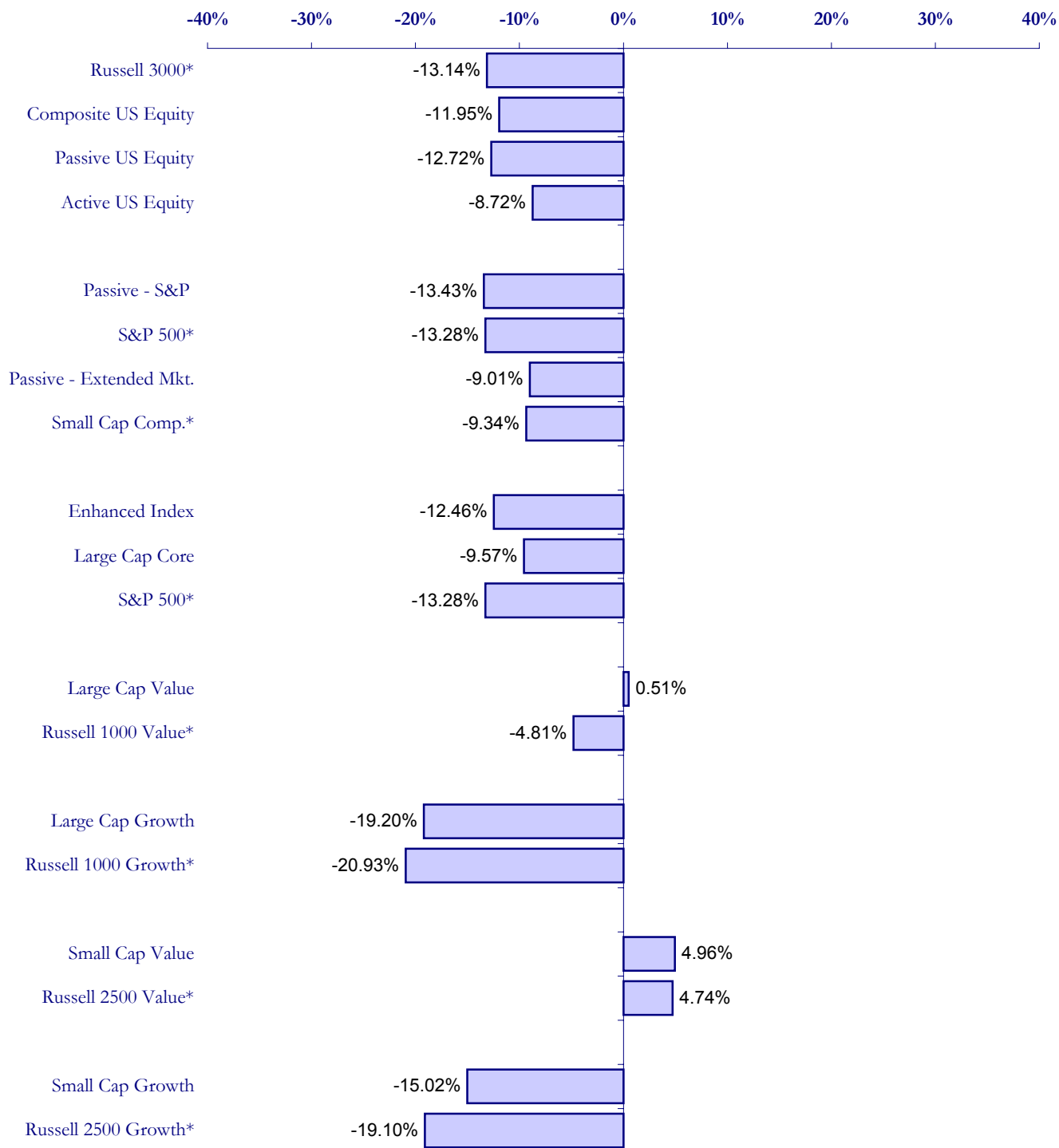
CalSTRS Active U.S. Equity Manager Structure

(Allocation based on the composite holdings of the U.S. Active Domestic Managers)

	Value	Core	Growth
Large Cap	31.9%	29.3%	31.5%
Small Cap	2.1%	2.9%	2.2%

U.S. Equity Portfolio

6 Months Ending June 30, 2002

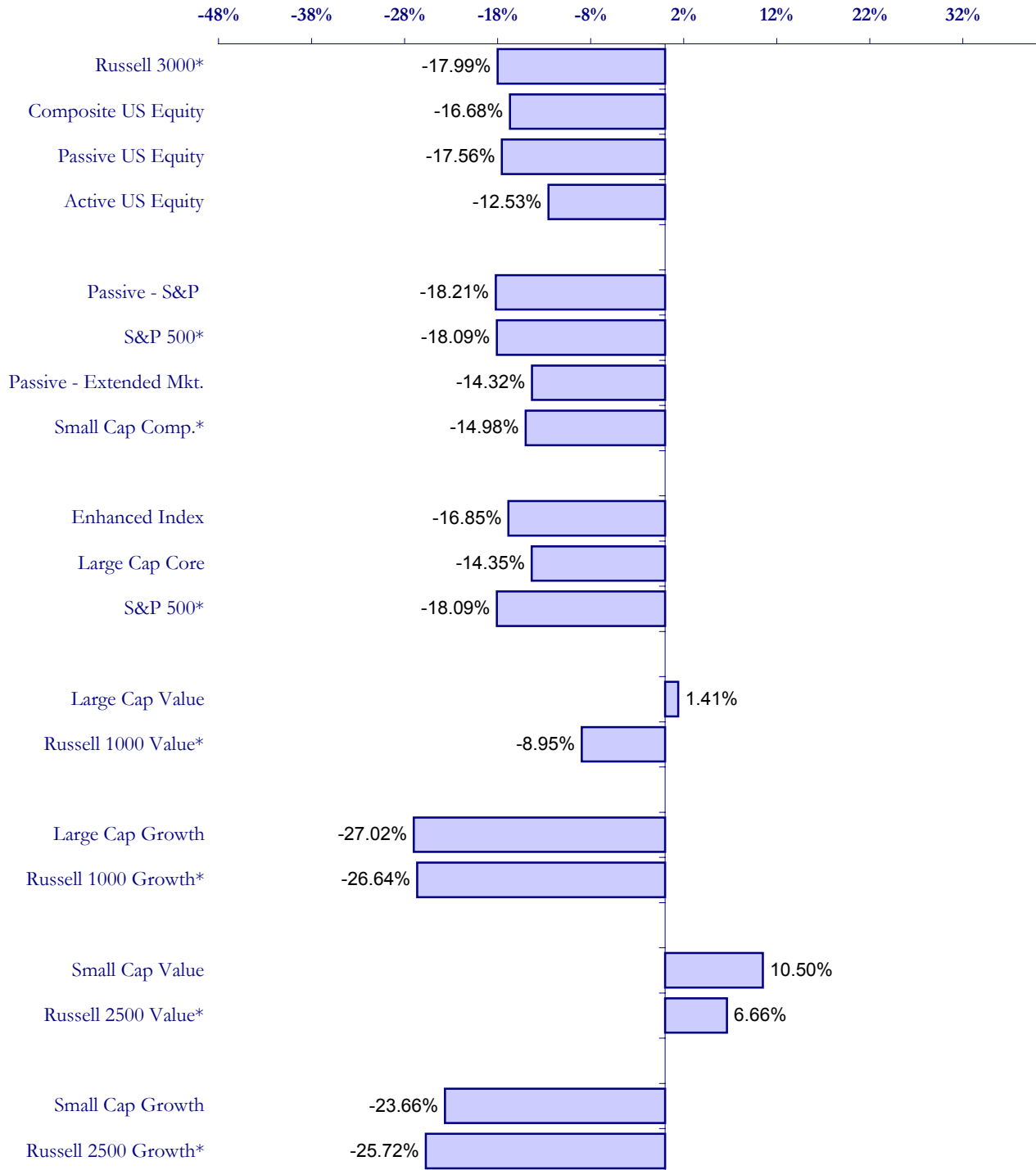


*Indicates the benchmark return



U.S. Equity Portfolio

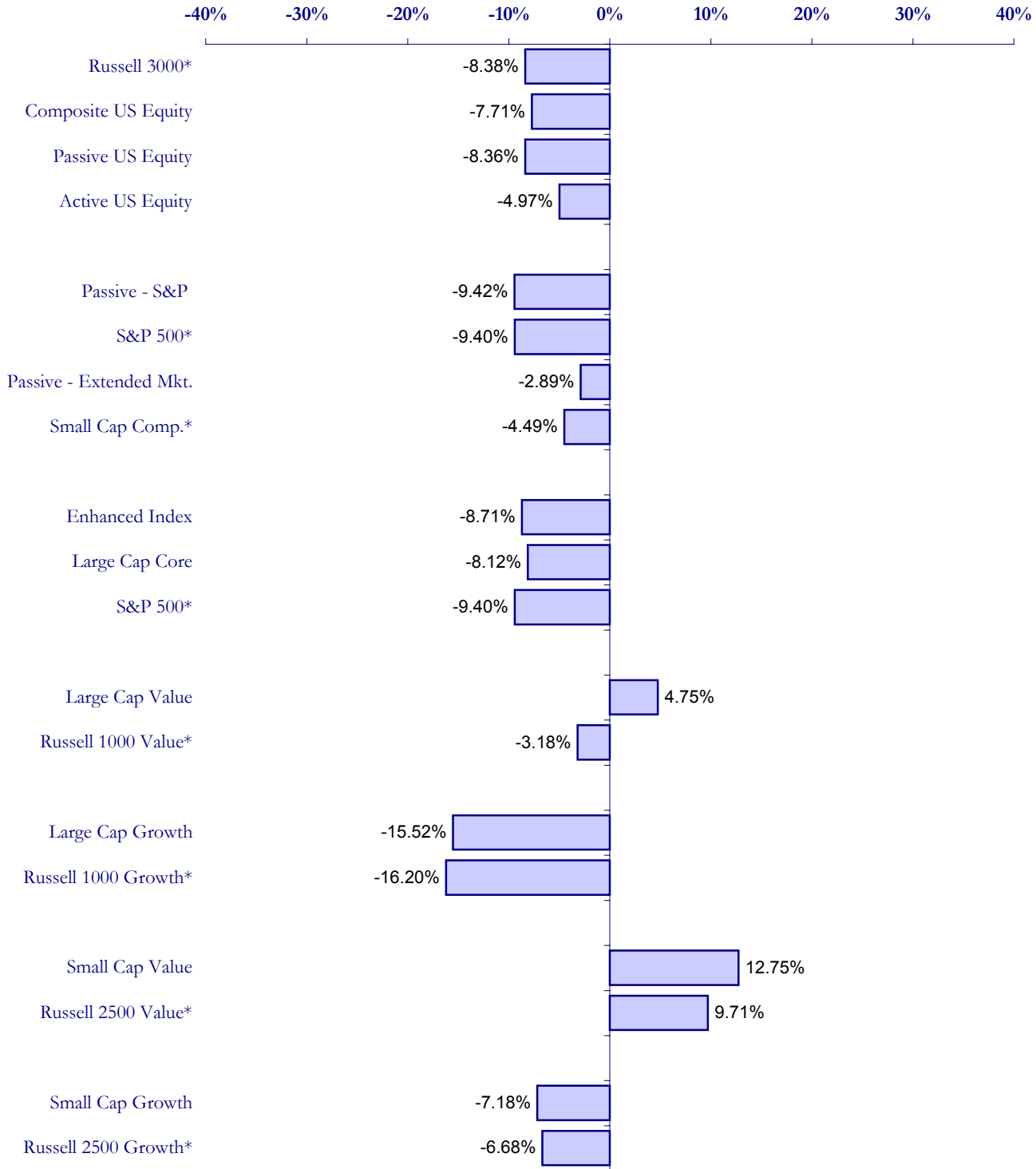
One Year Ending June 30, 2002



*Indicates the benchmark return

U.S. Equity Portfolio

Three Years Ending June 30, 2002



*Indicates the benchmark return



Non-U.S. Equity Portfolio Structure

MSCI ACWI free ex U.S. Structure

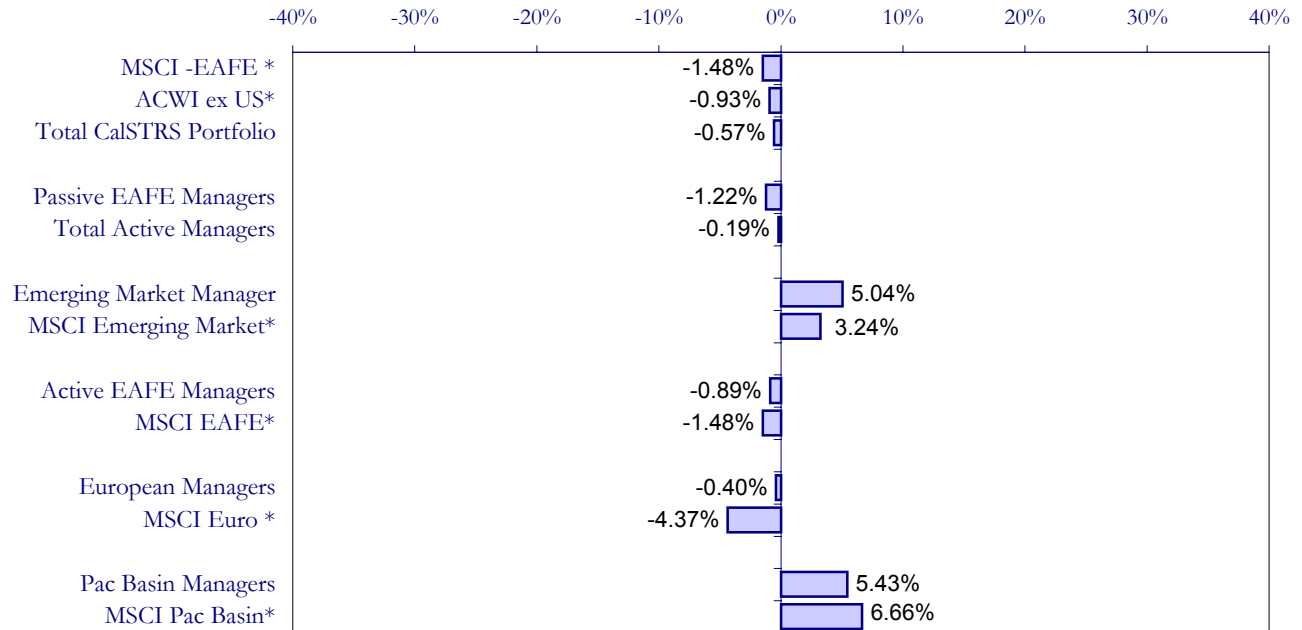
	Europe	N. America ex. U.S.	Pacific Basin
Developed Countries	62.4%	4.6%	25.0%
Emerging Countries	2.1%	1.4% L. America	4.6%

CalSTRS Active Non-U.S. Equity Manager Structure

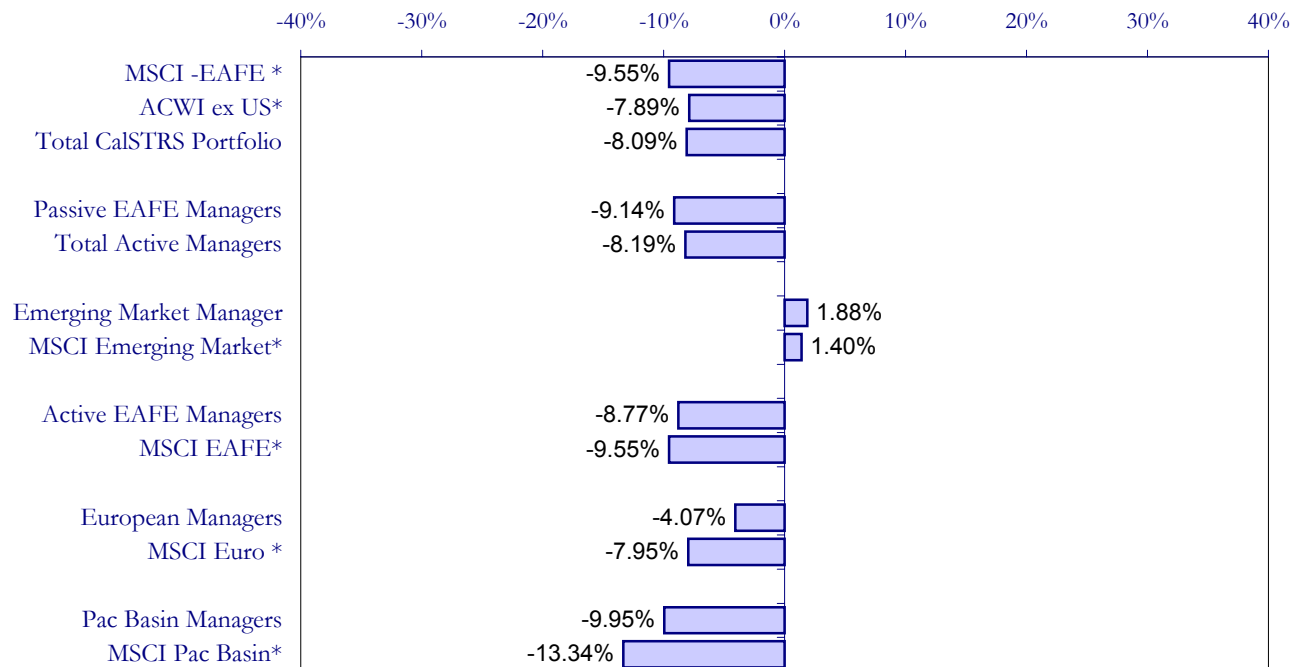
	Europe	N. America ex. U.S.	Pacific Basin
Developed Countries	66.4%	0.2%	29.5%
Emerging Countries	0.4%	0.7% L. America	2.7%

Non-U.S. Equity Portfolio

6 Months Ending June 30, 2002



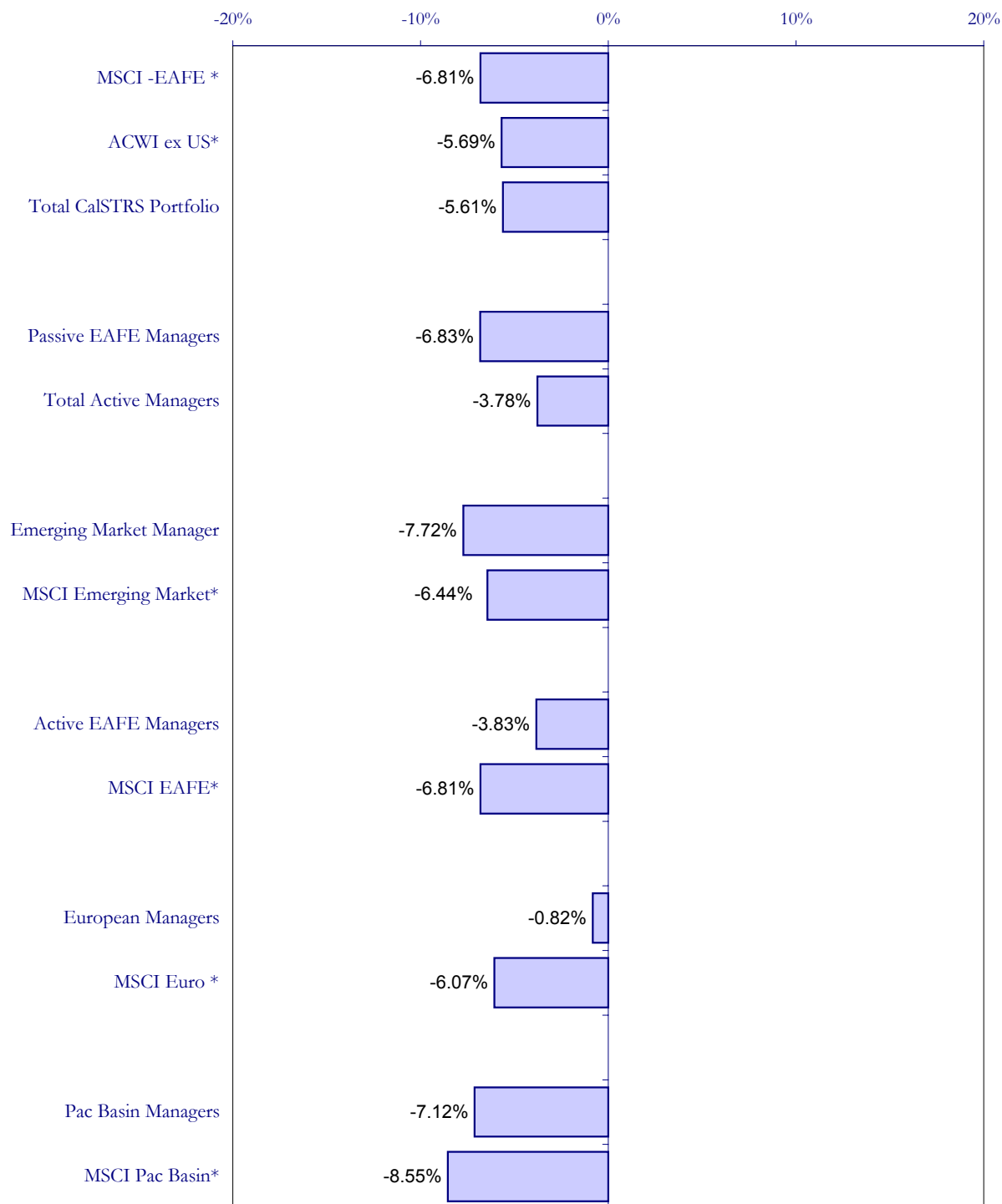
One Year Ending June 30, 2002



*Indicates the benchmark return

Non-U.S. Equity Portfolio

Three Years Ending June 30, 2002



*Indicates the benchmark return



Glossary

Passive Management – A method of managing an investment portfolio whose goal is to very closely replicate the return and risk characteristics of the desired index.

Active Management – A method of managing an investment portfolio that involves active selection of securities in an attempt to produce above-average returns on a risk-adjusted basis.

Capitalization- A description of the size of a corporation or stock. The capitalization is the outstanding shares of common stock times the price, plus preferred stock, retained earnings, and long-term debt.

Large Cap- (Large Capitalization stocks) The largest capitalized corporations within a given country. In the U.S., the Russell 1000, defined as the 1000 largest stocks based on the free floating shares as of May 31 each year. Large cap stocks have considerable retained earnings and a large amount of common stock outstanding.

Small Cap – (Small Capitalization stocks) The smaller capitalized corporations within a given country. In the U.S., the Russell 2000, defined as the 1001 to 3000 largest stocks based on freely floated shares as of May 31 each year. Small cap stocks are a relatively small firm having little equity and few shares of common stock outstanding.

Enhanced Index- An index that utilizes a technique called enhanced which makes relatively small adjustments to an indexed portfolio in order to increase the return slightly above the return on the index. Employing an enhanced method of investment style, the manager of an indexed portfolio may weight the portfolio slightly toward market sectors the manager feels are underpriced.

Growth Stocks – That are expected to have above-average increases in revenues and earnings. These firms usually retain most earnings for reinvestment and therefore pay small dividends or no dividends.

Value Stocks – That are expected to have consistent revenues and earnings. Value stocks usually retain most earnings for dividends, and value stocks emphasize asset value more than earnings projections.

Core Stocks – That are fundamentally neutral, neither growth nor value in investment style.

S&P 500 – An inclusive index made up of 500 stocks selected by a private committee. The index includes industrial, utilities, financials, transportations, and new economy corporations like AOL/Time Warner. The index also includes selective foreign corporations such as Royal Dutch Petroleum, Nestle. The index is constructed using market weights (stock price multiplied by shares outstanding, both publicly available and privately held) to provide a broad indicator of stock price movements. It does not represent the 500 largest stocks in the U.S. Index members constitute 85% of the capitalization of the U.S. stock market.



Glossary (continued)

Russell 3000 – A market-capitalization weighted U.S. equity index measuring the performance of the 3,000 largest U.S. companies based on market capitalization; this index represents about 98% of the U.S. equity market.

Russell 1000 – A market-capitalization weighted U.S. equity index representing the highest-ranking 1,000 stocks in the Russell 3000 Index; this index represents 80% of the total market capitalization of the Russell 3000.

Russell 2500 – A market-capitalization weighted U.S. equity index measures the performance of the 2,500 smallest companies in the Russell 3000 Index, this index represents about 20% of the Russell 3000's total capitalization.

STRS Russell Small Cap Completeness fund – The index consists of the companies in the Russell 3000 Index less the companies in the S&P 500 Index.

MSCI EAFE – The Morgan Stanley Capital Markets Inc. Europe, Australia, and Far East Index is a market capitalization-weighted equity index comprising 20 of the 48 countries in the MSCI universe and representing the developed stock market outside of North America.

MSCI ACWI ex US – The Morgan Stanley Capital Markets Inc All Country World Index is a market capitalization-weighted equity index comprising non-U.S. developed markets and emerging markets countries.

Developed markets – Defined by traditional index providers, such as the MSCI Index Committee, these are larger countries such as the United States that have a developed industrial base.

Emerging markets – Defined by traditional index providers, such as the MSCI Index Committee or the IFCI committee, as countries such as Mexico and Malaysia that are still developing their industrial base.

Pac Basin – The MSCI Pacific Basin Index is a capitalization-weighted index designed to track the performance of the developed countries in the Pacific Rim.

European – The MSCI Euro Index is a capitalization-weighted index designed to track the major countries in Europe. Benchmark containing stocks in ten EMU member countries plus the United Kingdom.

TUCS Universe - Trust Universe Comparison Services produced by Wilshire Associates. The universe compiles individual portfolio return from member pension plans, both public and corporate. For each given manager their rank is based on the portfolio of similar style.